

Exhibit D – Part II

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1 the opportunity to hedge out that risk all at once, then
2 he'll be -- he'll do more volume, he'll give you a fairer
3 price, all of these things, okay, so that if your option
4 trade was -- over-the-counter option trade was not just for
5 an option, or for an option with associated stocks, you might
6 be able to -- Madoff might have been doing something like
7 this.

8 So he might have been -- when he was buying and
9 selling his options, he may not have been selling them alone.
10 They may have been in conjunction with stocks. So then the
11 question is, if he -- if he was, and he wasn't, but if he
12 were doing it that way, why would the person on the other
13 side agree to stock prices which seemed so unfavorable to the
14 person on the other side?

15 So it didn't make any sense. But it was possible,
16 I mean. It's just that --

17 MS. STEIBER: But unlikely?

18 MR. LAUFER: But unlikely. In retrospect, it was
19 not so.

20 MR. KOTZ: All right. And so from your
21 perspective, you kind of knew enough to not -- that you
22 didn't understand it, that you just wanted to stay away from
23 it. Is that --

24 MR. LAUFER: Well, we were very worried. At the
25 end of the day, you have to speak to somebody else, how much

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1 we stayed away and stuff like that.

2 MR. KOTZ: Okay. But you were very worried because
3 you couldn't understand the process?

4 MR. LAUFER: That's right.

5 MR. KOTZ: But, you know, from a regulator's
6 perspective, would you say that what you saw could not
7 necessarily only be explained by front-running and there
8 might have been, you know, clues or possibilities beyond
9 front-running that would need to explain what you looked at
10 and couldn't understand?

11 MR. LAUFER: Yes. But that was only in conjunction
12 with a much larger portfolio than we had access to.

13 MR. KOTZ: Right. Right, right. But if you had
14 access, greater access, like a regulator would --

15 MR. LAUFER: Yes.

16 MR. KOTZ: -- then what you found would not
17 necessarily be solely explained by front-running?

18 MR. LAUFER: That's correct.

19 MR. KOTZ: And so, you know, I guess you have this
20 note, and you reference in the note something about,
21 "(Inaudible) would look pretty good above Elliott's" --

22 MR. LAUFER: I'm quoting Nat Simons.

23 MR. KOTZ: Right. Yes, yes. So, I mean, at that
24 point was there some sense that there was something illegal
25 going on, potentially?

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1 MR. LAUFER: I don't know. I don't remember.

2 Okay. What was also on our minds, or at least on my mind,
3 was that Madoff had been investigated --

4 MR. KOTZ: Right.

5 MR. LAUFER: -- and cleared. So we --

6 MR. KOTZ: By the SEC. Right?

7 MR. LAUFER: Yeah. So we had sort of assumed that
8 the regulators were busy looking into Madoff.

9 MS. STEIBER: Well, how did you hear this, that he
10 had been investigated and cleared?

11 MR. LAUFER: I heard -- I don't remember; this was
12 a long time ago. Okay. So I believe I heard that from Nat
13 Simons, I believe.

14 MS. STEIBER: And you heard "investigated" rather
15 than examined or --

16 MR. LAUFER: Oh, no, no, no, no. No, no. I don't
17 remember what I heard. It was my impression -- I was under
18 the impression, correct or incorrect, that Madoff had been
19 somehow examined and then something -- he had been
20 investigated. And I don't know what "cleared" meant, but he
21 had certainly never been indicted. There was never any
22 public mention that he had done anything wrong.

23 MR. KOTZ: And so is it fair to say that, you know,
24 from your perspective, you are under the impression that the
25 SEC had looked at it. You kind of go in with the assumption

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1 that there wasn't a problem there because the SEC had looked
2 at it.

3 MR. LAUFER: That's right. That's right.

4 MR. KOTZ: So you were --

5 MR. LAUFER: Also remember, Madoff had been
6 president of the NASDAQ.

7 MR. KOTZ: Right.

8 MR. LAUFER: And plus, from our viewpoint, he was a
9 good guy because it was generally our feeling that we get
10 better execution on an electronic exchange than the
11 specialist exchanges. And Madoff was -- or at least had the
12 reputation, which apparently is true -- of leading electronic
13 trading. So we liked that.

14 MR. KOTZ: But, you know, getting back to the SEC
15 part for a second, you know, your understanding is, you know,
16 there's a regulator involved. The regulator has much more
17 abilities and access to information than you had. And if the
18 regulator looked at it and didn't find anything, then that
19 would give you some comfort and make you maybe more likely to
20 go forward with an investment.

21 MR. LAUFER: That's right.

22 MS. STEIBER: Well, he (inaudible).

23 MR. LAUFER: Right. Right.

24 MS. STEIBER: Do you want to take a look at
25 (inaudible)?

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1 MR. KOTZ: Yes. If we could just -- there's a
2 couple of things on this e-mail you got that you might
3 remember.

4 MR. BARRON: You're looking at the --

5 MR. LAUFER: What do you want me to look at?

6 MS. PORTER: The one that says, "To new members:
7 We (inaudible) your concerns"?

8 MR. LAUFER: Okay.

9 MS. STEIBER: You said you were a committee member.

10 MR. LAUFER: Yes. I was definitely a committee
11 member here.

12 MS. STEIBER: What committee was that?

13 MR. LAUFER: Oh, (inaudible) the name.

14 MS. STEIBER: I'm just (inaudible).

15 MR. LAUFER: This one --

16 MS. PORTER: This did have a name.

17 MR. LAUFER: It did have a name? At any rate, this
18 possibly was the investment committee for Meritage.

19 MS. STEIBER: And what is Meritage?

20 MR. LAUFER: (Inaudible) what it was and what it
21 is. All right? So --

22 MS. PORTER: (Inaudible.)

23 MR. LAUFER: So I'm sorry.

24 MR. KOTZ: Take your time.

25 MR. LAUFER: Okay. So Renaissance: For a long

1 time, Renaissance's main investment vehicle and our only
2 product was the Medallion fund. At a certain point, the
3 Medallion fund -- for various reasons which I'll be happy to
4 expand upon, but my lawyers say no -- had more cash than was
5 needed to be kept at a brokerage company (inaudible).

6 Not that we had excess cash; at a certain point, we
7 actually had excess cash, but it started off with more cash
8 than was -- that the brokers -- there was more cash --

9 MS. PORTER: Can I stop you here? Forgive me for
10 saying this, but this is a much more complicated story and
11 it's a very short answer.

12 MR. LAUFER: Okay. Okay. Maybe you can give the
13 short --

14 MS. PORTER: No. I'm not on -- I'm not on the
15 record. I could give you --

16 MR. LAUFER: Okay. Meritage is essentially run by
17 Nat Simons for the purposes of being a fund of funds, and
18 otherwise manage money that is not in our main trading
19 system.

20 MR. KOTZ: Okay.

21 MS. PORTER: (Inaudible.)

22 MS. STEIBER: So it's a fund of funds.

23 MR. LAUFER: But there was one point when Meritage
24 was essentially a subsidiary of the Medallion fund.

25 MS. STEIBER: So the Medallion is a hedge fund, and

1 then Meritage is a fund of funds?

2 MS. PORTER: Yes.

3 MS. STEIBER: Okay. And who is David Zierk?

4 MR. LAUFER: He is somebody who works closely with
5 Nat Simons in Meritage.

6 MR. KOTZ: So there were a couple people that had
7 heard these concerns from ex-traders about Madoff.

8 MR. LAUFER: I presume.

9 MR. KOTZ: Okay. The information (inaudible).

10 MR. LAUFER: But that was not -- that was not from
11 me. That was from outside sources.

12 MR. KOTZ: Okay. Right.

13 MS. STEIBER: And what is the HCH?

14 MR. LAUFER: I believe the HCH was the name of the
15 investment we actually had in Madoff. And I don't remember
16 what HCH stands for or anything like that. But on the
17 Meritage balance sheet, you know, this is in General
18 Electric. This is in Microsoft. This is HCH. HCH was our
19 Meritage investment.

20 MR. KOTZ: Okay. This statement about, "Why does
21 he let us make so much money? Why doesn't he capture that
22 for himself?"

23 MR. LAUFER: Yes.

24 MR. KOTZ: What was that all about?

25 MR. LAUFER: You're asking? You don't know? I'm

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1 sorry, I --

2 MR. KOTZ: But I want to --

3 MR. LAUFER: Okay. So what are the big questions
4 about Madoff. So Madoff is managing these funds and
5 presumably doing a very good job of it, and charging very low
6 fees -- you know, Renaissance charges very high fees --
7 charging very low fees. You wonder, well, why is he charging
8 low fees? Maybe he's a nice guy.

9 But he is allowing other feeder funds to invest
10 with him who are charging high fees, or you might even --
11 from our viewpoint, what the industry charges.

12 MR. KOTZ: Right.

13 MR. LAUFER: So that made no sense to us.

14 MS. STEIBER: So explain why his fee structure was
15 unusual.

16 MR. LAUFER: There was no fee structure. He only
17 charged fees as a broker. If you have a managed account, and
18 normally you might pay a commission, or in his case, since he
19 was -- he was presumably collecting a bid/ask spread, there
20 was no explicit commission. There was -- so you received a
21 monthly statement, and it showed how much money you had.

22 MS. STEIBER: Now, but --

23 MR. LAUFER: So he didn't take a fraction of the
24 profits or anything.

25 MS. STEIBER: Right. How does a normal hedge fund

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1 structure its fees, basically?

2 MS. PORTER: Remember, he wasn't a hedge fund.

3 Okay.

4 MS. STEIBER: Okay.

5 MS. PORTER: Madoff was not a hedge fund.

6 MS. STEIBER: Madoff was not a hedge fund. But how
7 does a hedge fund usually structure its fees?

8 MS. PORTER: Okay. We on the hedge fund side have
9 a little sensitivity to be lumped in with Madoff.

10 MR. LAUFER: Right. So there is a management fee
11 and a performance fee. Typically, a management fee is a
12 certain fraction of the money of the management paid
13 quarterly over -- Renaissance charges quarterly. And then
14 every -- in our case, every six months you see if you made or
15 lost money. And if you've made money above previous losses,
16 a certain fraction of that is paid to the management.

17 MS. STEIBER: And you said that it was unusual that
18 he was paying -- or getting such a large percentage of the
19 money coming into the feeder fund.

20 MR. LAUFER: We don't know how much. We have no
21 idea how much.

22 MS. STEIBER: Okay. How much would a feeder fund
23 usually get when they --

24 MR. LAUFER: One in ten would be sort of typical.
25 I do not know what his feeder funds were getting. But a fund

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1 of funds, like Meritage, will charge a 1 percent management
2 fee and a 10 percent performance fee. That would be fairly
3 typical.

4 MS. PORTER: A typical hedge fund structure is more
5 a 2 in 20. A fund of funds is 1 in 10 because you're paying
6 the underlying funds as well. So it's a fee on top of a fee.

7 MR. LAUFER: But I did not know what fees the funds
8 feeding Madoff were charging.

9 MR. KOTZ: But he was leaving a lot of money on the
10 table?

11 MR. LAUFER: From our viewpoint.

12 MR. KOTZ: Right. And so given the volume that you
13 heard about, how much money are we talking about that he was
14 leaving out there?

15 MR. LAUFER: I don't know. You can do --

16 MR. KOTZ: But I mean --

17 MR. LAUFER: Do you want me to do the computation
18 in front of you? I'll be happy to.

19 MR. KOTZ: Sure.

20 MR. LAUFER: Okay. He was -- I haven't done this
21 before. Okay. I may make -- despite the fact that I'm not
22 (inaudible) errors. But let's assume he was managing
23 \$10 billion and he'd been making 10 percent. So \$10 billion,
24 he gets a 1 percent management fee, so that's \$100 million.
25 And he makes 10 percent, which is one billion. And he

1 charges 10 percent. So he's leaving \$200 million a year in
2 fees.

3 MR. KOTZ: Okay. And so -- and there was no
4 explanation that you could come up with as to why somebody
5 would do that? Is that fair?

6 MR. LAUFER: No. He was a good guy. I mean, no --
7 I'm going to repeat myself here. I'm sorry. You could say
8 that he thought whatever he was charging was appropriate, and
9 that was his business. But the fact he was allowing other
10 people to capture some of that --

11 MR. KOTZ: Right. Right.

12 MR. LAUFER: -- was the part that made no sense to
13 us.

14 MR. KOTZ: Right. Okay. I got you. Okay. And
15 then there was something else in this e-mail that you got
16 about "complicated business that could come to some
17 regulator's attention. Throw in that his brother-in-law is
18 his auditor."

19 MR. LAUFER: That's not my statements.

20 MR. KOTZ: Right. And I understand. I understand.
21 But this was shown to you or sent to you.

22 MR. LAUFER: Yeah.

23 MR. KOTZ: So what was your -- I mean, what was
24 your reaction to that? Did you have a concern when you
25 learned this information about the potential conflict?

1 MR. LAUFER: I don't remember.

2 MR. KOTZ: Okay. But what do you think about it
3 generally? I mean, would that be a red flag for you in terms
4 of when you look at something in this type of situation?

5 MR. LAUFER: Well, it would definitely be a red
6 flag. But, you know, it isn't as if every investment is
7 perfect. You've got to make some compromises here.

8 MR. KOTZ: Okay. Can you just explain --

9 MR. LAUFER: Incidentally --

10 MR. KOTZ: -- why it would be a red flag?

11 MR. LAUFER: Usually you want the auditor to be an
12 independent entity.

13 MR. KOTZ: Okay. And just to kind of clarify, when
14 you sent the e-mail, you say, "We have totally independent
15 evidence."

16 MR. LAUFER: Yes.

17 MR. KOTZ: What did you -- can you tell us
18 specifically kind of what you meant by independent?

19 MR. LAUFER: What I mean here is, very
20 specifically, that if you look at this -- if you looked at
21 those monthly statements and looked at the executions of the
22 stock side, that the prices were just too good from any mode
23 of execution that we were aware of that was legitimate.

24 MS. STEIBER: Too good to be true was your --

25 MR. LAUFER: (Inaudible.) I said, we do not know

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1 how to achieve executions anywhere near that using legitimate
2 methods. I'll repeat what I said before. If you looked at
3 Renaissance's performance from the outside, you would say it
4 was too good to be true from statistical analysis.

5 MR. KOTZ: And you quoted in your e-mail from
6 someone else, where it said, "If you're going to panic, panic
7 early."

8 MR. LAUFER: Yes.

9 MR. KOTZ: What did you mean by that?

10 MR. LAUFER: I said I quoted from Jim.

11 MR. KOTZ: Yes. I see. What did you -- what does
12 that mean? What does that quote mean?

13 MR. LAUFER: It means exactly what it means, that
14 if you're going to do something very rash, you're probably --
15 anyway, that statement, which is a semi-joke, all right?
16 It's (inaudible).

17 MR. KOTZ: No. I understand. I'm just trying to
18 understand it.

19 MR. LAUFER: If you're going to do something that's
20 rash, you're probably better off doing it before everybody
21 else does it.

22 MS. STEIBER: But "panic" is a strong word. It
23 sounds like those --

24 MR. LAUFER: When you think leaving -- you don't
25 think of leaving your investment with Madoff as panicking?

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1 MS. STEIBER: Well, it sounds like the red flags
2 that you're seeing are very strong if you are willing to
3 leave your investment.

4 MR. BARRON: Is that fair?

5 MR. LAUFER: First of all, this is sort of a joke.
6 I mean, it's a joke with some truth in it.

7 MS. PORTER: Yeah. This is -- he's quoting Jim,
8 and it's jocular.

9 MR. LAUFER: Almost (inaudible).

10 MS. PORTER: So don't put too much emphasis on the
11 word "panic."

12 MR. KOTZ: (Inaudible.) Okay. Sure.

13 MR. BARRON: Yeah. It's a generic comment. The
14 word "panic" might not necessarily be being applied to
15 Madoff, I think.

16 MR. KOTZ: Okay. And so after your internal
17 discussions, did anybody else get in touch with you from the
18 SEC or (inaudible)?

19 MR. LAUFER: No. Not me. Nobody from SEC ever
20 contacted me.

21 MR. KOTZ: Okay. But do you know if they contacted
22 other people?

23 MR. LAUFER: They may have, but I don't know.

24 MR. KOTZ: Okay. This is the other e-mail, the
25 April 20th, the longer e-mail. Do you have that? It looks

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1 like 2004, 2/12,

2 MR. LAUFER: I don't -- this is actually the first
3 time I've seen this one. I don't -- from -- I don't know the
4 names on top.

5 MR. KOTZ: Yeah. Because again, that was -- that's
6 the SEC people.

7 MR. LAUFER: Oh, okay. I may have --

8 MS. STEIBER: Paul Broder signed it.

9 MR. LAUFER: Oh, I think I may have seen this a
10 long time ago, maybe even recently. I may have -- okay. So
11 this is (inaudible).

12 MS. PORTER: Let me see a second.

13 MR. LAUFER: Okay. So you want me to read this?

14 MS. PORTER: Wait a second. You may not have
15 received this one. I think I have it in --

16 MR. LAUFER: I don't know. Sometimes I vaguely
17 remember, sometimes --

18 MR. KOTZ: If you could read it and just kind of
19 maybe explain it to me.

20 MR. LAUFER: Okay. I'm happy to take a while to
21 read it.

22 MR. KOTZ: Sure.

23 MR. LAUFER: Okay. (Examining.) Oh, yes. I think
24 I remember this one, only parts of it.

25 Okay. So the first call there is a computation of

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1 volumes, as I was saying to you. Okay? So the first part is
2 a computation of the -- is what I was describing the
3 summaries, as I had remembered and as was presented to me
4 since I said I don't feel like I'm an options expert.

5 And here Paul is doing some estimate of the
6 volume -- yeah. Paul is saying what I was summarizing to
7 you. He's analyzing the options that Madoff could have done.
8 His analysis was not the same as my analysis.

9 (Examining.) Yeah, No. 4. This what I was talking
10 about. "We have spoken to several market-makers in OTC and
11 (inaudible). None of them claim to see anything of this
12 volume in these options." Okay.

13 And then No. 5, Paul points out that there are many
14 options available, and somehow he always chooses the right
15 one, which might be very difficult to do if you're trading in
16 a very short time frame.

17 And the last -- next-to-last paragraph is also --
18 again, I'm quoting. This is -- this is not my own knowledge
19 I'm quoting, but Paul. My knowledge comes from Paul. Here.
20 Second page. "So we need an OTC counter party who was
21 willing to take a basket" -- so here Paul -- Paul was trying
22 to figure out how Madoff managed to do these large trades
23 that we don't know how he managed to do.

24 And he's suggesting what I was summarizing to you
25 before, that if you wanted to do a very large option trade,

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1 the reason why it's difficult to do is the person selling you
2 the option has this risk. And if you lower the risk that he
3 would have, he might do a very large trade with you over the
4 center.

5 One way to lower the risk is, at the same time you
6 buy the option, you do a corresponding stock trade. And that
7 will lower his risk. So Paul is saying that maybe Madoff did
8 the option trade and the stock trade with the same counter
9 party at the same time, which in some sense is theoretically
10 possible.

11 But then you ask yourself, why would somebody do
12 this? Because he's going to lose money doing the trade, so
13 far as we know.

14 MS. STEIBER: Right. And he seems to indicate,
15 with his exclamation points, that it's unlikely he would find
16 a counter party.

17 MR. LAUFER: For these very large sums.

18 MS. STEIBER: Right.

19 MR. LAUFER: But I'm quoting Paul here. But I
20 agree with his analysis entirely. But look, I can't resist.
21 This is not rocket scientists. This is not rocket science.

22 MS. STEIBER: Do you think that someone at the SEC
23 should be able to figure this out?

24 MR. LAUFER: Much more elementary than that.

25 Someone at the SEC could wander down, you know, to Goldman

1 Sachs and wander over to their options department and ask
2 them, how does somebody execute \$10 billion of options, and
3 find out it's very difficult. This is not --

4 MR. KOTZ: So how long --

5 MR. LAUFER: -- this is not proprietary -- this is
6 not proprietary Renaissance analysis here.

7 MS. STEIBER: It doesn't take your mathematical
8 background to figure it out. Is that what you're saying?

9 MR. LAUFER: Paul Broder would not claim to be a
10 mathematician, and he's an expert on this, and he's very
11 smart. But you don't have to be as smart as Paul Broder is
12 to do what he says here.

13 MR. KOTZ: So you think if a regulator got this
14 information, they could take some kind of basic elemental --
15 elementary steps to figure this out?

16 MR. LAUFER: Or ask some expert and tell them.
17 Don't do it themselves.

18 MS. STEIBER: Based on these three e-mails that you
19 have, if you were at the SEC, what do you think you would
20 have looked at? You'd look at options. What else? What
21 else do you think that you would have looked at if you were
22 given those three e-mails?

23 MR. KOTZ: If you were the regulator?

24 MS. PORTER: If you were the regulator and you had
25 the access.

1 MR. KOTZ: I'm asking you to pretend you're the
2 regulator.

3 MR. LAUFER: But this is -- you're not -- okay.
4 This is -- okay. Well, I do not claim to be an expert in
5 option trading. I claim I'm a, you know, above-average
6 layman. I claim to be somewhat of an expert in stock
7 trading.

8 If your SEC person had a small amount of expertise, it's
9 clear you go to Madoff and you say, show me the -- show me
10 your volume. Show me the counter parties. And you see how
11 he's managing to do these extraordinary things. You don't
12 have to figure out if he's front -- I mean, you don't have to
13 figure out if he's front-running or if he's doing something
14 weird. You ask him to show you what he's doing.

15 MS. STEIBER: What if he said, I am trading options
16 over the counter in Europe? I don't have documentation.

17 MR. LAUFER: I don't know. I'm not an auditor.
18 Let me -- and I apologize to my lawyers here. Okay. When I
19 was a 19-year-old, okay, so that was a long time ago, I got a
20 summer job in the company where my father worked where he was
21 (inaudible) chief scientist, if you like. It was a chemical
22 company.

23 And there was an audit going on. And I'm a
24 19-year-old I'm working in the library, you know. I'm a
25 secretary. This auditor says, you know, I have this invoice

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1 that says Schwarz Bioresearch bought \$20,000 worth of
2 chemicals from so-and-so, and my job is to make sure they
3 bought \$20,000 worth of chemicals from so-and-so.

4 Show me your piece of paper, your purchase order.
5 They call up so-and-so, and they check. And this was -- you
6 know, I'm 19 years old, but I see the auditor. All they're
7 doing is making sure that the pieces of paper in my father's
8 company show what's going on in the world.

9 Madoff says, I'm doing over-the-counter trades in
10 London, and the auditor accepts that? When I as a
11 19-year-old see this random auditor who is contacting some
12 small chemical firm? Let me give you another example.

13 Sorry.

14 So (inaudible), or you've gotten a government grant
15 to build a revetment. We're very pleased with this. It's a
16 million-dollar project. A million-dollar project, not \$50
17 billion. We're very pleased.

18 So a friend of mine, the mayor, who got the thing,
19 he said -- he's the former mayor -- he says, you know,
20 Michael -- the new mayor -- we will be audited on this. Not
21 we may be audited, we will be audited. Be sure and save all
22 the pieces of paper.

23 And you're telling me again that Madoff is going to
24 tell them, I did these trades in London, and they're going to
25 stop?

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1 MS. STEIBER: You think that that's doing a
2 thorough job?

3 MR. KOTZ: Okay.

4 MR. LAUFER: Now I can -- and now I can leave.
5 I've got that (inaudible).

6 MR. BARRON: Anything else?

7 MR. KOTZ: I think we've covered it.

8 MS. STEIBER: Is there anything else?

9 MR. LAUFER: (Inaudible.)

10 MR. KOTZ: Anything else that you can think of that
11 we didn't ask?

12 MR. LAUFER: No.

13 MR. KOTZ: Okay. All right. Thank you very much.
14 Appreciate your time.

15 (Whereupon, the interview was concluded.)

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RECEIVED

Testimony of Simons

Page 1

THE UNITED STATES SECURITIES AND EXCHANGE COMMISSION

In the Matter of:)
) File No. OIG-509
OIG-509)

PAGES: 1 through 51
PLACE: Renaissance Technologies Corporation
 800 Third Avenue, No. 34
 New York, New York 10022
DATE: Thursday, March 12, 2009

The above-entitled matter came on for hearing, via
videoconference, pursuant to notice, at 2:30 p.m.

TAPE TRANSCRIPTION

Diversified Reporting Services, Inc.

(202) 467-9200

1 APPEARANCES:

2

3 On behalf of the Securities and Exchange Commission:

4 DAVID KOTZ, Inspector General

5 HEIDI STEIBER, Investigator

6 Securities and Exchange Commission

7 100 F Street, N.E.

8 Washington, D.C. 20549

9

10 On behalf of the Witness:

11 FRANCIS P. BARRON, ESQ.

12 Cravath, Swaine & Moore LLP

13 Worldwide Plaza

14 825 Eighth Avenue

15 New York, New York 10019-7475

16 (212) 474-1000

17

18 CARLA PORTER, ESQ., General Counsel

19 Renaissance Technologies Corporation

20 800 Third Avenue, No. 34

21 New York, New York 10022

22 (212) 486-6780

23

24

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1 P R O C E E D I N G S

2 MR. KOTZ: Well, thank you very much for giving us
3 your time. We will try not to be too long. Let me just give
4 you a brief kind of background.

5 My office, the Inspector General's office, is
6 tasked with conducting an information of what occurred
7 between the SEC and its investigations, examinations, et
8 cetera.

9 Okay. So as I was saying, we're looking into all
10 the communications the SEC had relating to the Madoff matter,
11 and so various examinations and investigations that the SEC
12 conducted. And we're following up on all information that
13 they received.

14 There were some numerous tips. There was that
15 complaint that Harry Markopolos provided, which was a great
16 detailed matter. And in addition, there was some information
17 that they received in terms of your e-mails and other folks
18 in your office. And we're trying to understand exactly what
19 could or should have been done with respect to that
20 information.

21 So just to clarify, you know, we obviously see a
22 very different level of review and responsibility of you and
23 of the regulator. In your situation, obviously, you're
24 making investment decisions. It doesn't really go beyond
25 there.

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1 So I'm going to be asking you some questions that
2 go to, you know, what you think could have been done. That's
3 not necessarily to mean that you should have done it. It's a
4 question of, you know, what in your view should or could a
5 regulator h done.

6 Obviously, regulators have access to information.
7 There's a compulsory process, things like that. And so I
8 don't want to mean to imply that you guys are in the same
9 situation. But I do think it's helpful to understand, you
10 know, how you went about finding the information, what you
11 learned, what preliminary conclusion, if any, you drew from
12 that, and then what you might have done if you were sitting
13 in the regulator's shoes to follow up on the information that
14 they obtained.

15 So that's generally how I'm going to go through
16 this. I'll start out with some, you know, real short
17 background, then just really get into your recollections of
18 what you looked at at the time. We have an e-mail that
19 was -- that came from you. We may ask you a couple questions
20 about that. Okay?

21 MR. SIMONS: Okay.

22 MR. KOTZ: All right. Can you just tell me, you
23 know,, just for the kind of record, state your name?

24 MR. SIMONS: Nat Simons.

25 MR. KOTZ: Okay. And what's your current title?

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1 MR. SIMONS: Well, I guess -- it's kind of funny, I
2 mean, I'm (inaudible). And I'm also a director of Meritage.
3 I really manage -- I'm basically the manager of the Meritage
4 fund. So I'm (inaudible).

5 MR. KOTZ: Okay. Meritage fund is?

6 MR. SIMONS: It's an investment fund that is
7 primarily a fund of other funds, of other funds, brokerage
8 funds primarily.

9 MR. KOTZ: Okay.

10 MR. SIMONS: And -- although I've got other
11 activity, for example, an investment private equity fund, and
12 it does have direct investing activities as well. So we have
13 analysts that make direct investments in equities and
14 (inaudible), although at the time of the -- of that e-mail
15 and really over that time you're talking about, it was really
16 a (inaudible).

17 MS. STEIBER: And what was your position in 2003?

18 MR. SIMONS: I have managed Meritage from its
19 inception, which was in '97.

20 MR. KOTZ: Okay. And so when did you first hear of
21 Bernard Madoff?

22 MR. SIMONS: Well, probably really when I started
23 doing Meritage. It was '97, '98, that time frame.

24 MR. KOTZ: Okay. And what was -- did he have a
25 particular reputation, kind of, in the industry?

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1 MR. SIMONS: Yeah. I guess he had a reputation of
2 putting extremely consistent, you know, sort of low to mid
3 teens returns for the select few that could -- that could
4 get in.

5 MR. KOTZ: Okay. So there was a sense of
6 exclusivity?

7 MR. SIMONS: No question.

8 MR. KOTZ: And were there any whispers during that
9 time period or later about otherwise he was able to achieve
10 these returns?

11 MR. SIMONS: Certainly not at the time that I
12 became initially familiar. Now, again, let me -- let me
13 qualify that. I had not heard of him. I don't know, since I
14 wasn't really paying my attention, whether or not he had as
15 early as the late '90s, '97, '98, they were (inaudible).

16 And surely Madoff as a money manager goes back
17 quite -- I don't even know when he started managing capital,
18 if it was the early '90s. It was certainly a long time ago.
19 So there may well have been, even then, about the consistency
20 of his returns and perhaps how he could do it, but I wasn't
21 privy to that.

22 MR. KOTZ: Okay. But in terms of the exclusivity,
23 what was the sense of why he was so exclusive?

24 MR. SIMONS: Well, I guess the sense of why he was
25 so exclusive was there was the notion that whatever strategy

1 he was engaged in had, you know, capacity at some level. So
2 I think that the basis would have always been, you know,
3 not -- you know, inability to scale indefinitely the
4 investment strategy he was engaged in.

5 MR. KOTZ: All right. So then later on -- you
6 heard about him in '97, '98, but then later on there was talk
7 about trying to have some investment with him?

8 MR. SIMONS: Yeah.

9 MR. KOTZ: And so what happened with that? There
10 was a direct attempt that was not successful, or --

11 MR. SIMONS: That's right. Joe Simons, my father,
12 who had at least -- you know, did not -- really didn't know
13 or anything, but he had -- you know, they met. They had --
14 and of course, through the Simons Foundation and through the
15 (inaudible) Foundation, who was an investor, I guess he had
16 some at least ability to make a phone call, which he did.
17 But he was told in no uncertain terms that we couldn't
18 invest.

19 MR. KOTZ: And was there any reason given?

20 MR. SIMONS: Okay. I actually -- I thought -- I'd
21 be speculating if I said -- I think that question is probably
22 better asked of Jim. I mean, you know, it probably had
23 something to do with the fact that we were maybe a fund
24 manager ourselves, you know.

25 I mean, that's certainly an excuse, or a reason, I

1 should say, that people have given before. And so I
2 didn't -- it's sort of, why manage our capital, because
3 they're sort of managing a competitor's capital, if you will.

4 So I suspected it had something to do with that.
5 But the question (inaudible).

6 MR. KOTZ: And so then there was an effort made to
7 see if there could be an indirect attempt?

8 MR. SIMONS: Uh-huh.

9 MR. KOTZ: So how did that work?

10 MR. SIMONS: I'm sorry. (Inaudible.)

11 MR. KOTZ: So what did you do to try that?

12 MR. SIMONS: Well, we had -- from the beginning of
13 Meritage, we had a close working relationship with
14 (inaudible). And there -- our families go way back, back to
15 college, in fact. Jim Mayer (phonetic) and Joe Simons went
16 to college together at MIT. Lifelong friends. Early
17 investors. Both (inaudible) invested with, and we invested
18 early on in some of the enterprises that Jim Mayer was
19 involved with, and vice versa.

20 And Rafael Mayer, who's roughly my age -- in fact,
21 I went to school with Raf, went to high school with Raf -- it
22 was natural that we -- you know, since he was doing something
23 very similar to what I was doing, they said we would work
24 together. So we worked together very closely from the onset
25 because they had been doing it for longer than we had.

1 So we often exchanged notes about managers and, you
2 know -- and so, I mean, they had access to Madoff, and I
3 guess at some point -- I don't remember when -- we approached
4 them about possibly giving us an avenue in which to invest.

5 MS. PORTER: If I may step in one second.

6 MR. KOTZ: Sure.

7 MS. PORTER: You've heard in prior discussions
8 earlier of the name Khronos. Khronos is the corporate name.

9 MR. SIMONS: Yes. I'm sorry.

10 MS. PORTER: Khronos is the corporate name. They
11 have funds that they manage. So that's where Montpelier --
12 that's the name --

13 MR. SIMONS: Montpelier is their fund, their
14 corresponding entity which looks like Meritage.

15 MS. PORTER: And HGH is a subsidiary somewhere in
16 that -- in that fund family. But the connection here is the
17 Mayer family run the Khronos company, which is an investment
18 manager that runs these other funds.

19 MR. KOTZ: Okay. Thanks for that.

20 Okay. So there was this opportunity, and so then
21 you went about trying to decide whether this was a good
22 investment? Or what happened next?

23 MR. SIMONS: Well, yeah. I mean, certainly it was
24 difficult for us to go through our traditional methodology of
25 establishing, you know, the quality of investment. In this

1 case, I think that we felt that those standard channels were
2 not quite as important due to the nature -- due to the
3 transparent nature of the investment.

4 Obviously, most of the time you invest in hedge
5 funds, they're quite opaque. And therefore, you know, one
6 has to understand more carefully who you're dealing with. In
7 this case, I think the view was that Bernie was a very well-
8 known figure, high reputation. These activities were in a
9 managed account structure with complete transparency.

10 And so it was more a question of initially sort of
11 getting in as opposed to doing the sort of standard due
12 diligence. So it became more of a structural issue, I think,
13 than a diligence issue. At least that's how we saw it
14 initially.

15 MR. KOTZ: Okay. And so then what did you do, you
16 know, from a structural perspective? What did you do to try
17 to figure out what was happening with Madoff's operations?

18 MR. SIMONS: We didn't. I mean, from a structural
19 point of view, I only meant structurally setting up a
20 mechanism by which we could make investments.

21 MR. KOTZ: Okay. Okay. So --

22 MR. SIMONS: We did no due diligence, no extra due
23 diligence, as far as I remember, at that time because again,
24 we were already somewhat familiar with the investment
25 strategy because of the (inaudible) Foundation. I had worked

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1 with Raf, you know, before they -- before they had invested
2 with Madoff for many years.

3 And so it was -- I was trying to piggyback them, if
4 you will, on their due diligence and on the nature of the
5 investment, which was really quite different than other
6 investments that we (inaudible).

7 MR. KOTZ: Okay. So you didn't actually meet with
8 Madoff or really seek any documents from him.

9 MS. STEIBER: So what year was that that you made
10 your investment?

11 MR. KOTZ: Go ahead. So you didn't actually ever
12 meet with him or seek any documents?

13 MR. SIMONS: I never met with Bernie Madoff. I
14 never spoke to him. I have never spoken to him on the phone
15 or in person. I have never spoken to any people who work
16 within the Madoff institution.

17 MR. KOTZ: And you never got any documents from
18 them.

19 MR. SIMONS: Heidi, you asked a question.

20 MS. STEIBER: I said what year did you make the
21 investment, the indirect investment, with Madoff?

22 MR. SIMONS: I think it was '99. I didn't actually
23 go back and look. Did you check that, Carla?

24 MS. PORTER: Yes. It's not in our --

25 MS. STEIBER: And so when did you first have

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1 suspicions that you should look into Madoff more closely?

2 MR. SIMONS: Well, I think that -- first of all, I
3 want to put it in perspective. We started Meritage in
4 October of '97. It was myself, and I hired a guy who had a
5 masters in -- more than an MBA, it was a masters of
6 (inaudible) physics -- to help. We were managing a
7 relatively small amount of capital, and it was just me going
8 around and meeting a bunch of people.

9 As it went along, we built up more expertise. We
10 built up more internal analyst capability. And so, you know,
11 part of it becomes a situation where you sort of -- where you
12 have a better sense of what the opportunity cost is. Right?

13 So part of our discomfort with Madoff was just our
14 sense of the fact that we don't know, that we didn't know
15 that much about what they did and how they did it. And we
16 had better alternatives to invest in that we felt at least we
17 understood what the up side and the down side was.

18 So it wasn't just that we were starting to learn
19 anything more about Madoff -- because in fact, we really
20 weren't, you know, although, you know, I can certainly talk
21 about some of the things that we knew -- but, I mean, all the
22 things we knew, we didn't know that much more.

23 It was actually more getting a sense that, you
24 know, we're risking this thing that we don't really know to
25 make 12. We can actually make 12 pretty -- not to say pretty

1 easily; we were -- back then, making 12 didn't seem as hard
2 as it does today.

3 But back then, it felt like, why are we doing this?
4 Why are we taking this chance when we have a lot of other
5 good managers now. We have much better. (inaudible) so we can
6 get into just as much of that as anything else.

7 MR. KOTZ: Okay. And so in your e-mail, you talked
8 about speaking to ex-Madoff traders. Tell me about that.

9 MR. SIMONS: Well, we spoke to one. And I don't
10 even know if he was an ex-Madoff trader. He was somebody who
11 worked in some capacity there.

12 MR. KOTZ: Okay.

13 MR. SIMONS: And yeah. I mean, we actually
14 interviewed them, I think, for a position, you know. So it
15 was not -- it wasn't like we -- again, we didn't go out and
16 do due diligence on Madoff. It was just that we were looking
17 to hire another person within the Meritage organization.

18 But of course, you know, you work for Madoff, you
19 know we're invested in that. And naturally, you would ask
20 questions. And it was in that context -- and by the way, I
21 did not interview him, so this is all secondhand. But it was
22 in that context that those comments came out.

23 And, you know, this was somebody who had suspected
24 that they were somehow cherry-picking trades and -- which was
25 kind of consistent with what the sense was. You asked me

1 back in -- you know, when you asked me about rumors about
2 Madoff, I was responding to what rumors there might have been
3 just in the late '90s. And I really can't speak to any of
4 those.

5 But by the time we interviewed this person, which
6 was more like 2002, I believe, or 2003, there were -- I seem
7 to think (inaudible) that there were more rumors. And I
8 think the most common rumor that was out there was somehow
9 the notion that they were actively front-running their
10 institutional clients on the brokerage side.

11 And it was in that context, I think, that we put
12 the statement from that ex-Madoff employee.

13 MR. KOTZ: Okay. And then you said in the e-mail
14 that David Zierk heard a similar story. Who's David Zierk?

15 MR. SIMONS: David Zierk is -- David Zierk is
16 really -- he's worked at Renaissance, actually, since '96.
17 And he's worked on the Meritage activities since 2000. And
18 really, he's the guy right now who more or less on a day-to-
19 day basis manages the fund of funds portfolio.

20 And that was -- that was not entirely true back
21 then, but he was the most senior -- he's the most senior guy
22 on the fund of funds side that I have.

23 MR. KOTZ: And so what --

24 MR. SIMONS: And David probably is the one that
25 interviewed that person.

1 MR. KOTZ: Okay. And so that was a -- was that the
2 same interview, or was that a second one? Sort of from this
3 e-mail, it looks like -- you say, "David Zierk heard a
4 similar story from a large hedge fund consultant who also
5 interviewed an ex-trader."

6 MR. SIMONS: Oh, no. That is entirely different.
7 That is entirely different. And that was -- yeah. That was
8 a completely different event. Excuse me. Somebody is trying
9 to make a phone call here. We get this sometimes. That was
10 a completely different event, which again happened around the
11 same time that served to reinforce what we heard from that
12 person.

13 MR. KOTZ: So what was that other -- the second
14 event with David Zierk?

15 MR. SIMONS: That he was at a conference, and he
16 heard somebody who was working at a consulting firm make a
17 comment about how he was predicting a large -- you know, a
18 well-known manager potentially running into -- running into
19 regulatory problems.

20 And David more or less went up to the guy
21 afterwards and said, who were you talking -- somehow, from
22 the things that the person said, guessed that he might have
23 been referring to Madoff. The guy confirmed yes, indeed he
24 was.

25 MR. KOTZ: So when you say he heard that there

1 was -- he was running into regulatory problems, was that that
2 the SEC was looking at him or --

3 MR. SIMONS: (Inaudible) that he -- no, this is
4 somebody who suspected.

5 MR. KOTZ: That he would run into regulatory
6 problems or that there was some regulatory issue out there?

7 MR. SIMONS: No. He suspected that -- well, what I
8 would infer from that is that the person suspected that there
9 were existing ongoing irregularities that would at some point
10 be picked up by the regulators.

11 MR. KOTZ: Okay. I see. But had you heard about
12 whether the SEC had ever looked to Madoff's operations at
13 that point?

14 MR. SIMONS: No. The only thing that I know is
15 that we had -- you know, when we were -- well, we did have
16 discussions about making -- because again, obviously when you
17 do look at something like this and you have -- you know, when
18 you look at -- when you look at a situation where you feel
19 like you have complete transparency of the position.

20 You have none of the traditional risks associated
21 with the investment based on the position. There was no
22 undue leverage. There was no selling of premium that, you
23 know, (inaudible) some of the -- some of the concerns in
24 terms of the portfolio construction that one would want to
25 make sure weren't going to be issued that would step and, you

1 know, (inaudible) the investor weren't there.

2 So naturally, there was -- to make -- you know, one
3 of the issues that (inaudible) to make sure he didn't do
4 anything irregular with regards to his -- the other side of
5 his business, which was his brokerage business. And we did,
6 I think, know -- we were aware that on an even -- he had
7 been -- he had been investigated by the SEC, and (inaudible)
8 to develop.

9 I guess afterwards we did -- I don't know. I
10 remember hearing that we learned (inaudible) the brokerage
11 business, but we did think it was the whole business.

12 MR. KOTZ: You did think it was the whole business?

13 MR. SIMONS: We did but, you know, I mean, it's not
14 like we did exhaustive reach on it (inaudible).

15 MR. KOTZ: But at the time that you were, you know,
16 writing this e-mail, you were aware that the SEC had examined
17 Madoff, you know, in some capacity and given him a clean bill
18 of health?

19 MR. SIMONS: Correct.

20 MR. KOTZ: Okay. And so that led to your thinking,
21 well, if the regulators were there then, you know, you had a
22 little more confidence in his operation?

23 MR. SIMONS: Surely that helped to allay concerns
24 about that kind of -- that kind of risk. But again, now, my
25 comment had to do with the Attorney General, not with the

1 SEC.

2 MR. KOTZ: Your comment --

3 MR. SIMONS: When I made the comment that -- you
4 know, about Eliot Spitzer.

5 MR. KOTZ: Oh, yeah. Yeah. Okay. And so in the
6 e-mail, you also say -- I just want to read a little bit and
7 just see if you can elaborate on what you can remember.

8 "Another point to make here is that not only are we
9 unsure as to how HGH makes money for us, we are even more
10 unsure as to how HGH makes money from us, i.e. why does he
11 let us make so much money? Why doesn't he capture that for
12 himself? There could be a legitimate reason, but I haven't
13 heard any explanation we can be sure of."

14 MR. SIMONS: That was one of the biggest things as
15 far as I was concerned. We just hate to see situations which
16 are illogical, you know, on its face. I guess I didn't have
17 the imagination to think that the whole thing was just a
18 complete (inaudible).

19 But, you know, when you see a situation where it
20 would appear that he's only making money off of his -- off
21 the brokerage fees, why is he letting the Fairfield
22 Greenwiches of the world take 2 points? I don't know.

23 I mean, you know, and quite frankly, the only
24 thing -- again, that would lead you to the only kind of thing
25 that sort of makes sense, is this notion that, well, he's

1 really -- he's really front-running his institutional
2 clients, and this is the only way for him to -- he can't
3 really raise capital on that basis so he sort of does it in
4 this particular format.

5 And so, I mean, that's not the only solution, the
6 only explanation. But it is hard to understand why someone
7 who has -- supposedly has excess demand for his product
8 and -- you know, normally you see third party marketers in
9 situations where there is enough demand for the product.
10 Right?

11 They need the third party marketer to help them
12 raise the money. That's what they do. That's how they earn
13 their money. And they normally make -- they don't
14 normally -- you know, a pass-through fund. Normally you
15 take -- you know, you take 50 basis points or something,
16 right, or a hundred basis points.

17 So in this situation where it did appear that he
18 had excess demand and much of the money was coming in up
19 here -- apparently; again, very hard to see what was going
20 on, but through third parties -- it didn't make sense on its
21 face.

22 MR. KOTZ: So for you, that was a pretty big red
23 flag in terms of being cautious about going forward?

24 MR. SIMONS: Yes. And I think that that's the kind
25 of thing where, back in '99, it wasn't as evident. And I

1 don't even know back in '99, when we first made the
2 investment, I don't -- you know, I don't know how big
3 Fairfield Greenwich was. I mean, that was the most visible
4 and the largest aggregator of Madoff.

5 You know, you start to hear stories about how big,
6 you know, and those kinds of stories about like, you know,
7 gee whiz, is he really running 5-, 10, \$15 billion? Because
8 now, you know, lots of other things come into the picture too
9 that really weren't there in '99, I think.

10 MR. KOTZ: Like what?

11 MR. SIMONS: Again, going back to when -- you know,
12 why doubts started to come in in '02, '03, that weren't
13 necessarily there in '99. How do you ask that question
14 before? Again, it's when you start to get a sense of how big
15 he may be and (inaudible) because most things that we are
16 aware of do not scale at that level. And then you start to
17 wonder again how somebody can continue to do that.

18 MR. KOTZ: Okay. And so in addition to the fact
19 that, you know, there was kind of money left on the table, so
20 to speak, there was this point you make about how there's a
21 \$4 billion Madoff pass-through fund, Fairfield Century, that
22 charges 0 to 20 percent. It's not clear why Madoff allows an
23 outside group to make \$100 million per year in fees for doing
24 absolutely nothing.

25 And so just give me a little bit of elaboration on

1 that. What did you mean by that?

2 MR. SIMONS: Well, again, (inaudible) normally are
3 required to help fundraise fees, raise fees, raise
4 (inaudible). You are effectively outsourcing your -- you
5 know, your investment relations, you know, (inaudible), your
6 sales and marketing.

7 In Madoff's situation, when there -- you know, it
8 appeared that there was plenty of pent-up demand for his
9 product, which would mean that you just kind of hire a couple
10 of guys and set them up in offices, and you could raise money
11 all day.

12 And so why not just capture that for yourself,
13 build your own IR, you know, sales and marketing team in-
14 house? Why continue to outsource it to Fairfield?

15 MR. KOTZ: And so in your case, he was actually,
16 you know, kind of pushing people away who wanted to invest,
17 and here this entity was getting all this money for nothing.

18 MR. SIMONS: Right. I had to jump through hoops to
19 get in.

20 MR. KOTZ: Right. Okay.

21 MS. STEIBER: Did you have any suspicions at the
22 time of why he would do something like that? Did you think
23 he was avoiding regulation?

24 MR. SIMONS: So again, you know, sometimes people
25 do things for historic reasons. Right? You know, you work

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1 with someone. They've come into this thing, and you're doing
2 fine and they're doing fine. And maybe there might be -- you
3 know, you want to see goodwill. Right?

4 And sometimes, you know, it's not like all hedge
5 fund managers are trying to write their own local economics.
6 Right? That's fine. I personally think that that's a smart
7 thing. I think hedge funds play it too close to the -- you
8 know, too close to the edge, and then all they need is a
9 small draw-down and the next thing you know, they could be
10 out of business.

11 So there -- you know, we thought, well, maybe there
12 was -- maybe that was that. But like I said, the other thing
13 which -- again, the concern was that there was somehow --
14 because of his underlying business, because of the fact that
15 he was somehow using his order flow on the brokerage side to
16 benefit his clients with managed accounts, that that was
17 something where he couldn't raise money in a hedge fund
18 structure for that, or he didn't want to have the money
19 directly.

20 And therefore, you know, these third parties served
21 this purpose of creating this, I don't know, you know, buffer
22 between him and the capital. I mean, that was the only sort
23 of -- again, besides just goodwill and besides historic
24 relationships and everything else, maybe he didn't -- maybe
25 he was making enough and he didn't really feel like he needed

1 to capture every dime. But it did appear that the economics
2 were pretty focused towards the -- towards the fund.

3 But of course, you don't really know. Right? I
4 mean, you can't get under the hood. Right? So maybe there
5 was some underlying agreement between Fairfield and Madoff,
6 and maybe some of that could come back to him. Right? Maybe
7 he had an interest in Fairfield. Maybe he was a GP, you
8 know. It's hard to know, when you can't go down there
9 tomorrow, what's really going on.

10 MR. KOTZ: Okay. And then the next point you talk
11 about is, "We don't know why he does what he does. We have
12 no idea if there are conflicts in his business that could
13 come to some regulator's attention. Throw in that his
14 brother-in-law is his auditor and his son is also high up in
15 the organization, and the risk of some nasty allegations,
16 freezing of accounts, et cetera, et cetera."

17 So what did you -- what did you mean by that?

18 MR. SIMONS: Well, you know, we had -- I guess
19 talking about family members, I mean, there had been other --
20 I think Mariposa down in Florida is an example of a -- of a
21 fund that was engaging in -- you know, in illegal activities,
22 where there were a lot of family members around.

23 Of course, I don't have anything against family
24 members working in the same organization. But clearly, when
25 you're dealing with a more closely held organization like

1 that, where a large percentage of the people who are working
2 at the top of the organization are in the family, that
3 creates a better environment -- creates an environment that's
4 more ripe for abuse.

5 So that was the first thing about family members.
6 And obviously, the auditor being a brother-in-law, well, I
7 mean, you know, you'd want -- the auditor serves a pretty --
8 and I don't even -- by the way, that may not be right,
9 because I think they did have -- that statement might have
10 been wrong. But I knew that there was people close up in the
11 accounting group, and you really want to see good separation
12 there.

13 MS. STEIBER: So (inaudible) from the auditor,
14 whether it be a brother-in-law or not, you wrote this in the
15 e-mail. And if someone from the SEC were reading the SEC,
16 you would expect that they would look at the auditor, based
17 on your e-mail. Right?

18 MR. SIMONS: If you're asking me whether or not the
19 SEC should have taken an e-mail like that seriously if it was
20 brought to their attention in terms of if I -- you know,
21 sure, if there had not been previous activity around that, if
22 this was like some -- you know, if the SEC weren't already
23 aware of these issues.

24 MR. KOTZ: Right. And you even say that their
25 concern was it would come to some regulator's attention, and

1 then there would be an impact on the operation. And then
2 this did come to a regulator's attention. Right?

3 MR. SIMONS: Yes, it did.

4 MR. KOTZ: Okay. And then at the bottom you do
5 make this comment about, "Madoff said it would look pretty
6 good above Eliot Spitzer's mantel." I know that's in jest,
7 but what was kind of the point there?

8 MR. SIMONS: I thought it was kind of funny. It
9 was at the time. It ceased to become funny when you guys got
10 the e-mail.

11 (Laughter.)

12 MR. SIMONS: You know, Eliot Spitzer was cracking
13 down on managers. I mean, this is -- I think this was around
14 the time of the -- a lot (inaudible). Right? And I really
15 put that sort of in a similar bucket.

16 I mean, we were thinking about mutual fund market
17 timing and the issues around that, even though I didn't refer
18 to that in my e-mail. But I was thinking about that in the
19 context of Madoff because it was sort of that level of
20 irregularity that we were thinking about.

21 We were thinking, again, maybe he's doing something
22 illegal because he's front-running his clients and giving his
23 clients bad prices. And just like -- just like mutual fund
24 market-timing, where the result of a mutual fund market-
25 timing is effectively a tax on the buy and hold mutual fund

1 owners, right, with people that are getting in and out, and
2 are really, because of the way that mutual funds operate, you
3 know, are getting in and out at -- with basically no
4 slippage.

5 So that, you know, it's more like -- I don't
6 know -- I don't know how familiar you guys are with that
7 issue. But it's a similar issue because mutual fund market-
8 timers would often go in and out of small cap funds, and
9 small cap funds tend to trend, right, because mutual fund
10 managers, if they decide to buy a small cap fund, they can't
11 buy it all in one day because they move the market too much.
12 So they buy it over multiple days.

13 So if we started to see a move-up in the small cap,
14 sometimes in a (inaudible) small cap company, you can
15 actually buy a mutual fund and take advantage of that;
16 whereas if you have to go and buy and sell the underlying
17 stock, your slippage would kill you and you wouldn't make any
18 money.

19 And because of that, you can make a lot of -- you
20 can actually make money. And what it is, basically it's an
21 unrealistic price being bought and sold by the people that
22 are getting in and out. And again, it comes out of the hide
23 of the people that just own the small cap fund throughout.

24 So it's a tax on the buy and hold. And I saw this
25 as potentially a very similar issue, where Madoff was

1 effectively taxing the institutional clients, pension funds
2 or anything else, for the benefit of his -- of his managed
3 account clients.

4 And so I was concerned that Spitzer was going to
5 come after him and make an example of him the same way that
6 he made an example of this mutual fund market-timing.

7 MR. KOTZ: Now, this e-mail did make its way to the
8 SEC. Did anybody from the SEC contact you and ask you any
9 questions?

10 MR. SIMONS: No.

11 MR. KOTZ: So nobody followed up at all with you?

12 MR. SIMONS: Nope. And I would have remembered if
13 somebody had done it.

14 (Laughter.)

15 MR. KOTZ: Okay. And so you were at that point
16 proposing that you guys get out entirely?

17 MR. SIMONS: Well, certainly at the time of that
18 e-mail, I was making the argument that we should get out. I
19 was making the argument that we should get out. Now, we
20 have -- or had, I should say; we don't have that structure
21 any more, but we did then -- an investment committee, and the
22 investment committee would make collective decisions about
23 the investments that we made.

24 I managed the fund, and we made the
25 recommendations. But the recommendations -- and they were

1 generally followed by the committee, but the committee, you
2 know, voted on it and, you know, if two people didn't want to
3 make the investment or (inaudible), you know, we acted
4 accordingly.

5 And so there was certainly not uniformity in terms
6 of the view on Madoff at that time, again, because we weren't
7 really contemplating that it was a Ponzi scheme. And when we
8 were given the -- when we basically were able to put -- you
9 know, so we're able to -- we reduced our risk, is the bottom
10 line. We took half our equity out. And we didn't eliminate
11 the position because there wasn't, again, like I said,
12 uniformity of opinions as to how to proceed.

13 MR. KOTZ: Do you think that the fact that the --
14 that you were aware that the SEC had looked at it and kind of
15 given him a clean bill of health, do you think that had any
16 impact on the decision not to completely take all your
17 interests away?

18 MR. SIMONS: Yes. Yes, I do. Not just that, but
19 because of the nature of the fact that these were brokerage
20 statements, and he had a big broker dealer business and big
21 market-maker and -- you just assume that someone was paying
22 attention to make sure that there was something on the other
23 side of the trade.

24 MR. KOTZ: And there were other issues that
25 referenced by Paul Broder in another e-mail having to do with

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1 options. Did you have any -- what did you -- what was that
2 all about? What were the specifics there that you can
3 recall, the other concerns?

4 MR. SIMONS: Sure. We were making estimates. We
5 were making suppositions about how large he might be. And we
6 were making -- based on -- you know, based on some attempts
7 to aggregate information that we had in terms of Fairfield
8 and other feeder funds that we were aware of.

9 So first you sort of make an estimate of a range,
10 and then you say, well, let's say the top end of that range
11 (inaudible). And now let's make -- let's take a look at the
12 managed account information that we had. And now it's
13 assumed that he's manages all that other -- all those other,
14 whether they're accounts or whether they're pass-throughs,
15 let's assume that he basically manages it like a pool.

16 What does that tell you -- what does that tell you
17 if those assumptions were in fact true? What does that
18 indicate about the size of his OEX position? And it was in
19 that context that that concern was raised because if you did
20 assume that it would be (inaudible) the range, if you did
21 assume that everything was done on a 5 to 2 basis, it doesn't
22 work, you know. The old interest is not big enough to
23 (inaudible) that position.

24 You know, I mean, there are other ways. You know,
25 there are all kinds of potential flaws -- or not flaws,

1 potential places where you could be wrong. You could be
2 wrong on the size of the overall book, you know, in terms of
3 how much money he's managing, again, not a knowable number.

4 You could be wrong about the fact that all the
5 positions -- all the books were managed in lockstep because
6 again, you don't know that. You don't know to what extent.
7 There could be very different return (inaudible) associated
8 with an account; we can't see them.

9 And the third thing is you may or may not -- you
10 know, there is always an over-the-counter situation because
11 there's quite a lot of over-the-counter volume in equity
12 options, in equity (inaudible) options. So he could have
13 been using over-the-counter positions for parts of his book.

14 So it was really not the size of his, but again,
15 it's just another thing that makes one uncomfortable.

16 MR. KOTZ: Was there an effort made to see if he
17 was using over-the-counter for that much volume and
18 positions? Did you guys look at that?

19 MR. SIMONS: No. There's no -- right.

20 MR. KOTZ: Yeah. I mean, Paul Broder sent an
21 e-mail that indicate that, you know, that was looked at. Do
22 you remember that?

23 MR. SIMONS: I don't think that -- well, I know --

24 MR. KOTZ: In terms of the counter party?

25 MR. SIMONS: I don't see how -- I mean, look. I

1 don't -- I mean, you've obviously already talked to Paul. I
2 don't know how one would have gone about looking to see if
3 something was done over the counter. I mean, you can't go
4 and talk to Goldman Sachs and (inaudible) and say, are you in
5 a big over-the-counter derivative from Bernie Madoff? They
6 would tell you to, you know, whatever.

7 So I don't even know how we would have gone about
8 trying to ascertain that. You know, I think -- look. We
9 live in the listed -- you know, in the listed exchanges. So
10 I think that -- you know, I can't recall any efforts to try
11 to delve into the over-the-counter market (inaudible).

12 MS. STEIBER: Is there a way for him to read this
13 e-mail there to maybe refresh his memory about what Paul had
14 done that he relayed to him in this e-mail?

15 MS. PORTER: Oh, we can certainly do that. It'll
16 take a little time to get it --

17 MS. STEIBER: Maybe we'll just read --

18 MR. SIMONS: If you might (inaudible).

19 MS. PORTER: You know, remember that Nat's the fund
20 of funds manager, and Paul manages the trading desk. So
21 their experiences are very different. So Nat may not know
22 substantively what Paul is talking about.

23 MR. SIMONS: Now, and I also want to point out,
24 guys, that they were doing some things with regards to Madoff
25 that had nothing whatsoever to do with Meritage, you know.

1 And so Paul was looking into some things, and he wasn't
2 necessarily relaying -- he obviously relayed to me about
3 like, you know, we'd talk about the size of the OEX position
4 that it would be, and I was aware of all that. But he may
5 not have relayed to me information about what they were doing
6 over the counter.

7 MS. STEIBER: Well, let me read to you this section
8 of this e-mail that he sent to you that's specifically about
9 the over-the-counter reach to see if it triggers any memory.

10 He said, "When we examined the issue before, we
11 concluded that maybe he does the options in the OTC market.
12 We have spoken to several market-makers in OTC equity
13 options. None of them claim to see any significant volume in
14 OEX options. Recall that Raf stated that Madoff said it was
15 necessary to spread trades over several days. Why, if you
16 were doing over-the-counter," and then he (inaudible).

17 MR. SIMONS: I see, so -- okay. No. I do -- I
18 guess, I mean, I should have read that; obviously, a little
19 more closely before coming here. Look. It makes sense, I
20 guess. If you can really -- if it's the case, I thought that
21 there were larger volumes in the OTC market. So obviously,
22 at the time, I'm sure I knew that, but I just forgot.

23 So yeah, okay. So I guess what he basically -- he
24 wasn't looking into whether Madoff had positions like that.
25 He was looking into whether Madoff could have positions like

1 that. I mean, just talk to the major market-makers in OTC
2 options.

3 MR. KOTZ: Right.

4 MR. SIMONS: So that just -- anyway, so there are
5 other ways. I mean, remember that if you were -- I'm just
6 wondering if -- and I have to -- well, anyway. It is what it
7 is.

8 MS. STEIBER: Let me read the next point. Recall
9 point 2. "This would indicate that the over-the-counter
10 options would also have to be done at the end of the day to
11 get a strike near the close. Are we to believe that the
12 market-makers would take on 15 billion of market risk at the
13 close?

14 "Of course they might," and then he puts might and
15 three exclamation points, "be willing to take the option risk
16 if Madoff provided the market hedge in the underlying, i.e.
17 they did the whole package with Madoff. But we already know
18 that the trades in the underlying compared with the closing
19 prices would lead the over-the-counter counter parties
20 showing losses, as our account always shows gains."

21 And then he says -- his last point is, "Of course,
22 all of our trades are with Madoff as the principal, so our
23 option positions are over the counter with Madoff, so he can
24 choose to use any strike and any total volume he chooses, but
25 the risk must be covered somewhere if he is doing these

1 trades at all.

2 So we need an over-the-counter counter party, not
3 necessarily a bank, who is willing to do the basket of the
4 options plus the underlying with Madoff at prices unfavorable
5 for the over-the-counter counter party. In 10- to 15
6 billion," three exclamation points.

7 MR. SIMONS: Right. So I certainly understand that
8 point. And it's a good point because basically, that goes
9 back to the fact that we observed that he got extraordinarily
10 good fills, which again points to the notion.

11 And so if you have to -- of course, if you have to
12 do the trades more or less at the same time and if you have
13 to go with the same counter party -- because they're never
14 going to be willing to do something like that on a naked
15 basis; they need to be hedged -- then yes, how do you -- how
16 would you do that? How would the counter party be willing to
17 take those losses? Yeah. I mean, that's certainly a very
18 good point.

19 MS. STEIBER: So would it be fair to say that based
20 on the e-mail that you received, that the research that
21 Renaissance had done concluded that he really wasn't trading
22 over the counter, or it was very unlikely that he was trading
23 over the counter?

24 MR. SIMONS: Well, I don't know. I guess so. You
25 know, if they concluded -- I mean, I think that it certainly

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1 pointed to the difficulties that he would have in transacting
2 heavily on -- you know, over the counter. But I don't think
3 that Paul was trying to say that it wasn't possible.

4 Again, he was making the assumption about the size.
5 15 billion was at the outside of where we thought he might
6 be. So we were again saying he would -- if he's running
7 15 billion and if he's trying to do what (inaudible), you
8 know, a lot -- a large percentage of that over the counter,
9 it would be hard. It would.

10 MR. KOTZ: So if you were a regulator, you were in
11 the regulator's shoes, and you got information like this, you
12 know; what steps would you take, do you think, to look into
13 this further?

14 MR. SIMONS: So again, I guess I'm going to make
15 the assumption that I was unaware up to this point that there
16 may be a problem (inaudible). So this is somehow -- this is
17 like, I'm new to this game. I never heard of Madoff. I
18 get -- I get some information about this. I don't have any
19 contacts (inaudible) further.

20 Look, I guess I would go down -- if I really
21 thought that this came from a credible source and if this
22 work were being done at a high level by smart people, I would
23 presumably go down to the office and some questions about --
24 you know, about the nature of what he's doing and how he's
25 doing it, and show me the other side of your trades, and all

1 that good stuff.

2 MR. KOTZ: So what if you -- so there would be ways
3 for you to determine, for example, whether he was trading
4 over the counter by perhaps talking to counter parties?

5 MR. SIMONS: I guess. I mean --

6 MR. KOTZ: Okay. And so if you went to Madoff and
7 he said, I do my trading in Europe, how would you react to
8 that?

9 MR. SIMONS: Yeah. I mean, I guess I would say,
10 well, (inaudible). I need to see the other side of those
11 trades in Europe. If they're in Europe, that's fine, but
12 you're doing them with someone. There's got to be somebody
13 on the other side of the trade.

14 Again, you're asking me questions, though, that I
15 don't know to the extent -- the extent of the jurisdiction of
16 the SEC. I mean, I'm assuming that you have the ability to
17 extend beyond country borders, if it's an American operation,
18 to see what they're doing.

19 MR. KOTZ: Okay. Putting aside the jurisdictional
20 issue, there are things that could have been better?

21 MR. SIMONS: Well, strictly from the point of view
22 of just being the practical issue, then, you know, that's not
23 sufficient (inaudible).

24 MR. KOTZ: So is it fair to say that when you guys
25 looked at it, you thought there was something potentially

1 wrong sufficient that you were uncomfortable, but you hadn't
2 really made any conclusions of whether it was front-running
3 or something else; but it was kind of enough to just simply
4 say, we got an issue here?

5 MR. SIMONS: Remember, Madoff makes (inaudible) the
6 order of 12 or 13 percent. That's what we were doing in our
7 portfolio outside of him.

8 MR. KOTZ: Right.

9 MR. SIMONS: It wasn't like he was boosting our
10 returns. The thing that was so great about Madoff was the
11 smoothness of the returns.

12 MR. KOTZ: Right.

13 MR. SIMONS: But if you had a reason to believe
14 that there was an embedded (inaudible) inside of those
15 returns, for some reason then the volatility number that you
16 have is no good. And we see that a lot.

17 You know, one of the -- you know, we used to invest
18 in a lot more funds where they would show these smooth
19 returns, and a lot of the standard way to manage those smooth
20 returns is by trading fixed income (inaudible), right, where
21 they have a lot of control over the marks, so that basically
22 they just -- they average the bid and the ask.

23 I mean, they don't do anything illegal, but they
24 have a lot of flexibility over the mark because they have an
25 over-the-counter security. And in that situation, you know,

1 the return -- you know darn well that the volatility that the
2 manager is showing you isn't real.

3 Now, again, here we were dealing with what we
4 thought were managed -- what we believed were managed
5 accounts with complete transparency in terms of the trade,
6 and dealing with exchange-traded securities, which means that
7 that argument doesn't work. Okay.

8 So the volatility that you were seeing should be
9 true with the underlying volatility. But if there was some
10 other risk associated with it that could not be quantified,
11 then you couldn't justify being inside of the trade purely on
12 the basis of risk/reward, it starts to go completely against
13 you because he's not making 25 percent a year.

14 MR. KOTZ: So, I mean, you obviously didn't
15 identify any fraud. But it's apparent to say that from what
16 you saw, there was at least a potential that there was fraud
17 here?

18 MR. SIMONS: When you say fraud, you mean -- you
19 mean like -- you don't mean front-running your clients. You
20 mean -- I just want to make sure (inaudible) before I --

21 MS. PORTER: What do you mean by fraud?

22 MR. KOTZ: Yeah. I would me, you know, fraud like
23 not trading or some other thing other than just front-
24 running.

25 MS. STEIBER: Auditor lack of independence, you

1 know, getting false audits, something like that.

2 MR. SIMONS: You know, again, I think the best
3 evidence -- the only real evidence, I think, of fraud, the
4 only real -- I shouldn't say evidence; the only real
5 indication that there may be fraud, I suppose, at least in my
6 mind, was the OEX information.

7 But there, again, we just had no way of knowing
8 whether those other accounts looked like this one. And so we
9 really -- I never, as the manager, entertained the thought
10 that it was truly fraudulent. And, you know, perhaps I
11 should have. But I didn't.

12 And it again was because, I think, of a combination
13 of the fact that it appeared that the idea of fraud -- it
14 would have been so -- again, it would have been so easy to
15 prove that it was fraud if it was just managed accounts that
16 were set up. It would have been so -- again, forgive me
17 here, but, you know, it would have been pretty
18 straightforward.

19 We felt that he was sufficiently in the eye of the
20 regulators that it was just hard for us to envision that that
21 was the case. And so then you'd fall back into these second
22 order concerns.

23 MR. KOTZ: When you say pretty straightforward,
24 pretty easy, you mean pretty easy for a regulator like the
25 SEC. Right?

1 MR. SIMONS: I guess I mean that. I mean --

2 MS. PORTER: He doesn't understand.

3 MR. SIMONS: You know, I --

4 MS. PORTER: Nat, you can be free.

5 MR. BARRON: Go ahead. You can say it.

6 MS. PORTER: You can be free. You can say it.

7 It's okay. They won't take it personally.

8 MR. KOTZ: I mean, our job is to try to figure out
9 what happened so we can improve things. So we are dying to
10 hear what people think.

11 MR. SIMONS: I had had -- I had met three managers
12 personally who went to jail after I met them. Okay? We,
13 happily, did not invest in any of them. But they went
14 physically behind bars, and they were -- they were
15 fraudulent.

16 But these were -- they were -- they were all kind
17 of elaborate schemes, and they involved private (inaudible),
18 and they involved all these kinds of like okayed structures.
19 I had never seen something that looked on its face to be so
20 transparent that in fact was fraudulent in the way that
21 you've described.

22 And so I guess I was given a false sense of
23 security by the nature and the structure of Madoff that the
24 likelihood of it being an out-and-out scam was quite -- was
25 quite low.

1 And, generally speaking, scams tend to be smaller.
2 Right? These funds that I saw were 100 million, 200 million.
3 You know, we'd never seen a multi-billion-dollar fraud
4 before. Generally speaking, my view has been that it's hard
5 to multi-billion-dollar frauds to happen because it involved
6 the complicity of so many different people. And so it is
7 hard to pull off.

8 So I guess we felt, again, you know, with being
9 such a public figure, being -- having such -- you know, being
10 a large -- you know, a large market-maker, all the other
11 activities, the idea of out-and-out fraud struck me as just
12 too far-fetched.

13 I mean, I'm sorry, it didn't strike me. It was
14 probably too far-fetched for me to get my arms around, which
15 is why it never really occurred to me, which is why I wasn't
16 pounding the table at that time saying, we have to get out
17 entirely because I'm not going to -- you know, we think that
18 there's a possibility of fraud. You don't -- you don't leave
19 half your capital at risk.

20 Even at that time, it was like 2 percent. So we'd
21 have to have (inaudible). That's not -- you know, we're
22 trying to make 14 percent. A 2-1/2 percent loss is pretty
23 dramatic.

24 MS. STEIBER: Did there come a time when you
25 heard -- you (inaudible) e-mails where you heard other rumors

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1 that made you want to reduce your position even more than the
2 50 percent that you had reduced, or that you heard other
3 rumors that were more serious?

4 MR. SIMONS: No. You've pretty much -- that
5 e-mail -- that e-mail was the culmination of hearing these
6 things. And there was nothing that came to my attention that
7 was of a different nature, at least not that I remember. It
8 was obviously a fairly long time ago. They wanted to
9 (inaudible).

10 MR. KOTZ: So in the end, there were significant
11 funds that were lost because positions were left in after it
12 came out in December?

13 MR. SIMONS: No. We were out -- we were out about
14 a year after that e-mail. But again, I do have to go back
15 over this because I don't -- you know, I don't remember
16 precisely what the terms were. But more or less my
17 recollection is that we were -- we were kicked out
18 (inaudible).

19 MR. KOTZ: Kicked out by?

20 MR. SIMONS: By HGH. At the time, we were
21 redeeming them from our funds. As you probably know, we
22 had -- Medallion had lots of outside investors. You know, we
23 kicked them all out by the end of '05.

24 They were large outside investors, our largest
25 outside investor, and they needed really to put -- you know,

1 to get that money back to work. So certainly didn't put it
2 on payoff, I think. But that was -- you know, they
3 basically -- they basically felt they needed the capacity.

4 And so I didn't even finally, at the end of the
5 day, decide (inaudible), which they had, in order for them to
6 look a little smarter.

7 MS. STEIBER: So my final question. If you had the
8 e-mails that you know that you sent and the other e-mails
9 that you received about the strange options activity, if you
10 were a regulator and you investigated the possibility of
11 front-running and didn't find anything, do you think that
12 would have satisfied all of the concerns raised in those
13 e-mails?

14 MR. SIMONS: So if I were a regulator and I looked
15 into the particular allegation of front-running and I didn't
16 find any basis for that, to justify that claim --

17 MS. STEIBER: If I didn't find front-running.

18 MR. SIMONS: I didn't find front-running -- would
19 that have -- would I have felt that I didn't need to go any
20 further?

21 MS. STEIBER: Right. That's the question.

22 MR. SIMONS: No, because there were two other
23 key -- you know, two other key points. Well, I guess the --
24 you know, the main key point was obviously the OEX position,
25 the OEX option position, because the other -- I guess the

1 three components was good fills, big OEX option position,
2 and what appears to be a predictive -- you know, ability to
3 pick the S&P.

4 I suppose you can't question somebody's ability to
5 pick the S&P. I suppose if they can pick the S&P, they can
6 pick the S&P. More power to them. So I suppose it's the OEX
7 position that would be the other thing you would want to take
8 a look at.

9 MS. STEIBER: What about the auditor independence
10 issue?

11 MR. SIMONS: (Inaudible.)

12 MR. KOTZ: So it's fair to say that even if front-
13 running was ruled out, the questions weren't fully answered,
14 and one would have to continue to look to see how these -- to
15 look at these potential red flags?

16 MR. SIMONS: Yeah. But let me tell you one other
17 thing, I guess, and I -- just -- well, you probably know
18 this. Right? But you asked -- actually, I'm going to go
19 back.

20 You asked me a question before about whether or not
21 I'd heard anything else. And I should -- I should probably
22 say that the only other thing was I had heard -- and I
23 believe I had actually already heard that, but I don't really
24 remember the timing -- was that there was a restricted floor
25 within -- you know, within their activity, within their

1 organization. There was some floor or some section of a
2 floor or something that was -- had restricted access.

3 MR. KOTZ: And so that would be also something to
4 be concerned about in terms of secrecy?

5 MR. SIMONS: The auditor, and independence, and
6 making sure the accounting is -- yeah. I mean, there are
7 restricted -- people have, you know, restricted floors,
8 things like that. But it is a red flag. Right?

9 MR. KOTZ: All right. I think that's all we have.

10 MS. STEIBER: Thanks, Nat.

11 MS. PORTER: Thank you, Nat.

12 MR. KOTZ: Thank you very much. We appreciate it
13 very much.

14 MS. PORTER: Thanks, Nat. Did you -- oh, you have
15 a question?

16 MR. KOTZ: Sure.

17 MR. SIMONS: I figure I get one question.

18 MR. KOTZ: You can have as many questions as you
19 want.

20 MR. SIMONS: Well, again, I'm just curious. I
21 think I understand from some conversation, I don't know, that
22 these e-mails triggered some investigation. I mean,
23 obviously that may not be the only investigation that Madoff
24 (inaudible), and I -- but I'm just curious.

25 Are you guys -- are we particularly distinguished?

1 Or are you talking to lots of folks who have had -- who, you
2 know, -- who, for whatever reason, there was some interaction
3 between them and the SEC that might have prompted, you know,
4 (inaudible)?

5 MR. KOTZ: Yeah. There are -- there are definitely
6 other folks. And I think that, you know, some of the other
7 folks, like Harry Markopolos, provided, you know, a very
8 detailed, you know, 25-page complaint to the SEC asking for
9 action, then trying to follow up with them.

10 So, I mean, they're in a very different category
11 than you guys, in which just some e-mails kind of got to the
12 SEC's attention. And then there are others who are in
13 somewhat of a similar situation to yours. And there's been
14 numerous -- and this is relatively widely reported, so I'm
15 not giving anything away -- but there have been numerous
16 pieces of information that were brought to the SEC's
17 attention.

18 So you are not distinguished in that way, and
19 you're certainly not distinguished in that, you know, while
20 they got hold of some of your internal e-mails which you
21 looked at for a different purpose, it wasn't comparable to
22 the scale upon which somebody actually came to the SEC
23 specifically and said, this is what's going on. It may be a
24 Ponzi scheme. Here's why. Please call me.

25 So I guess that's why. But I mean, it is certainly

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1 a part of the puzzle. But, you know, the report will focus,
2 you know, I think quite a bit more on other aspects of it,
3 particularly since the Harry Markopolos matter prompted the
4 investigation, in which you have more authority and ability
5 to find a Ponzi scheme, while your areas prompted more of the
6 kind of examination/review side.

7 But nevertheless, we are kind of looking at all the
8 issues to see, you know, to the extent that these things were
9 brought to the SEC's attention on more than one occasion,
10 similar type issues, consistent views in terms of the
11 appearance of red flags kind of combined all together, why
12 weren't certain things done that seem to us to have been able
13 to determine that this was a Ponzi scheme or that he wasn't
14 trading or, you know, going beyond kind of looking at the
15 front-running issues.

16 MR. SIMONS: Okay. And I guess, you know, just the
17 last sort of thing I would sort of say (inaudible), you know,
18 we invest in other funds. Yet certainly we would like to
19 believe that the SEC is helping to make -- to ensure that
20 these funds are not fraudulent.

21 So clearly, we're sort of on the same side of the
22 thing. I'm the only guy that you've talked to that directly
23 oversees activity that invests in other managers, right, so
24 that we effectively (inaudible). I mean, I see where you
25 talked to investors in the fund that we manage, but they

1 don't do it on a daily basis.

2 So it's certainly -- you know, I want you to know
3 that clearly we're certainly happy to provide an opportunity
4 to help. And I guess the last thing is, you know, I think
5 maybe one of the reasons why, by the way, just in terms of --
6 if you did -- there is sort of the underlying question which
7 is, you know, did it ever really occur to you to call the
8 SEC, you know, why didn't you ever call the SEC, or all that
9 kind of thing.

10 We did feel that despite the fact that we're kind
11 of smart people, we were just looking at matters of public
12 record. I mean, you know, it wasn't hard to get these
13 statements. These statements, you know, hundreds of -- lots
14 and lots and lots of people had Madoff statements.

15 So we didn't really feel that we were dealing with
16 something which is proprietary, and therefore the conclusions
17 that we came to were something that was -- you know, other
18 people were unlikely to come to. And it's not like we
19 needed a PhD in mathematics to do the -- to do the study on
20 the OEX. Right? I mean, this is just -- just looking at the
21 size of the market.

22 So, you know, I just have to say that, I mean, I
23 think -- I almost think that, I mean, you know, maybe now, I
24 suppose, if there was a Madoff II floating around and some of
25 these things were out there, people would think twice about

1 it because our imagination is that much greater.

2 But, you know, anybody else, I just don't know how
3 one would have expected to -- you know, to go and call the
4 SEC about anything like that. And it's not that we wouldn't
5 want to be good citizens and helpful, you know, because it's
6 not in anybody's interest to see this kind of thing happen.
7 And obviously, there's great damage to our industry and to a
8 lot of -- to a lot of, you know, good people.

9 MR. KOTZ: Right. Now, I agree with that. But I
10 think on the other side, there has to be a confidence level
11 in the SEC. So for example, you know, you can't really take
12 the position, I don't think, in this case that, you know,
13 this one should have come forward and that one come forward
14 because I don't think -- you know, Harry Markopolos did come
15 forward. He provided a 20-page document. He followed up.
16 And, you know, it still wasn't found.

17 MR. SIMONS: When did he first come forward?

18 MR. KOTZ: Well, I don't want to go into too many
19 details. But --

20 MR. SIMONS: Oh, I'm sorry. I thought that was a
21 matter -- I wasn't asking for anything that wasn't a matter
22 of public record.

23 MR. KOTZ: No. I mean, the document that's out
24 there on the internet is 2005, and there were some efforts
25 prior to that as well.

1 MS. STEIBER: He testified before Congress that he
2 first came forward in 2000. So that's public.

3 MR. KOTZ: Okay. Yeah. So --

4 MR. SIMONS: I thought that -- I certainly don't
5 mean to ask you anything that's internal.

6 MR. KOTZ: No, no, no. So yes. So, I mean, he
7 did, and then in 2005, as he testified, there was, you know,
8 a pretty thick document provided with a lot of information.
9 And so, you know, there has to be a feeling that the SEC
10 will, once it's brought to its attention, find it.

11 And the thing that I was asking you about before
12 that concerns me is I do think that there are people out
13 there who relied on the fact that the SEC looked at it and
14 didn't find anything.

15 And, you know, so it's almost as if, you know, it's
16 kind of bad enough that they didn't find it; but it almost
17 would have been better if they hadn't looked at it because if
18 they hear they looked at it and didn't find, then that
19 provided a level of comfort to people that wouldn't have been
20 there if they hadn't looked at it at all.

21 But, you know, I mean --

22 MS. PORTER: A false sense of security.

23 MR. KOTZ: Right. So, you know, we need to kind of
24 understand how this could have happened, and then learn from
25 it and look at, you know, why it is that they were unable to

1 uncover this; and then, you know, look at possible
2 solutions -- training, you know, other possible ways, so that
3 they can be kind of in the same situation as you folks were,
4 you know, even in your very limited review, which you didn't
5 really need to go any further for.

6 But if you had kind of, based on that expertise,
7 been at the SEC, one would think that there were things that
8 could have been done relatively easily that could have then
9 uncovered this, you know, massive scheme.

10 MR. SIMONS: Yup. Well, listen. Obviously, it's
11 in our interests to make you guys -- not make you guys -- for
12 a nice, strong, you know, well-functioning SEC in this
13 regard. So if there's anything we can do, anything I can do
14 to follow up, happy to, you know, answer further questions.

15 MR. KOTZ: Okay. Great. Well, thank you very much
16 for your time.

17 (Whereupon, the interview was concluded.)

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